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**MEDIUM TERM
MICROFINANCE DEVELOPMENT STRATEGY
IN THE KYRGYZ REPUBLIC
2006-2010**

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List of Abbreviations

ADB	–	Asian Development Bank,
WB	–	World Bank,
GDP	–	Gross Domestic Product,
SHG	–	Self Help Group,
GTZ	–	German Development Cooperation Agency,
EBRD	–	European Bank for Reconstruction and Development,
EU	–	European Union,
CB	–	Commercial Banks,
CU	–	Credit Unions,
CSF	–	close-end joint stock company micro credit company “Cooperative Stabilization Fund”,
KAFC	–	close-end joint stock company “Kyrgyz Agricultural Finance Corporation”,
IMF	–	International Monetary Fund,
MERCY CORPS	–	Mercy Corps Women’s Microcredit,
MCA	–	Micro credit Agency,
MCC	–	Micro credit Company,
MFI	–	Institutions rendering microfinance services,
MFC	–	Microfinance Company,
MFO	–	Microfinance Organization,
NGO	–	Nongovernmental Organization,
NFCI	–	Non-Bank Financial and Credit Institutions Licensed by the National Bank of the Kyrgyz Republic,
MSFF	–	Micro and Small Enterprise Finance Facility of European Bank for Reconstruction and Development,
UNDP	–	United Nations Development Program,
SSC	–	Open-end Joint Stock Company “Settlement and Savings Company”,
CIS	–	Commonwealth of Independent States,
TACIS	–	Technical Assistance for the Commonwealth of Independent States,
NBSD	–	Non-Bank Supervision Department of the National Bank of the Kyrgyz Republic,
FINCA	–	Foundation for International Community Assistance,
FCSDCU	–	“Financial Company for Support and Development of Credit Unions in the Kyrgyz Republic” Limited Liability Company,
CAMFA	–	Central Asian Microfinance Alliance established by ACDI/VOCA and Foundation for International Community Assistance (FINCA),
CEE	–	Central and Eastern Europe,
USAID	–	United States Agency for International Development,
ACDI/VOCA	–	Agricultural Cooperative Development International/Volunteers in Overseas Assistance,
CGAP	–	The Consultative Group to Assist the Poor – a consortium of 28 public and private foundations jointly operating to expand the access of the poor to microfinance services in developing countries
DCCA	–	A non-governmental organization of the Kyrgyz Republic “Development and Cooperation in Central Asia”,
DFID	–	Department for International Development of the United Kingdom,
IDA	–	International Development Association, member of the

World Bank Group,

- IFAD – International Fund for Agricultural Development,
- PEARLS – Early warning system of risks for credit unions (P- Protection, E- Effective financial structure, A- Asset quality, R- Rates of return and costs, L- Liquidity, S- Signs of growth),
- SECO – Swiss Secretariat for Economic Development,
- SWOT- analysis – Analysis of Strengths, Weakness, Opportunities and Threats,
- WOCCU – World Council of Credit Unions

1. Introduction

In view of the rapid growth of the microfinance sector, the National Bank of the Kyrgyz Republic initiated the development of a Medium Term Microfinance Development Strategy in the Kyrgyz Republic (hereinafter referred to as the Strategy). This Strategy is focused on the efforts of the Government, financial sector, in particular, MFIs (hereinafter referred to as MFIs) and other interested parties towards building a dynamic and sustainable microfinance sector, since a sustainable microfinance sector with increased capacity to render services to a wide range of urban and rural public will result in the improvement of economic level and reduction of poverty. In order to eliminate circumstances hindering the development of this sector and take appropriate measures to improve the legal and regulatory environment, an assessment of the existing legal framework for microfinance has been conducted for taking corrective actions to make it more attractive for financial institutions to work with the poor and to expand their activities in remote regions of the republic.

The development of the Strategy is particularly important in view of the fact that the year 2005 has been declared as the International Year of Microfinance. The Kyrgyz Republic is the first country among countries of the Central Asian region that developed a microfinance development strategy.

The Strategy was developed by the National Bank of the Kyrgyz Republic and representatives of the microfinance sector with the financial support of the FIRST Initiative Company and technical assistance from FACET BV group of consultants, the Netherlands.

In the course of developing a draft Strategy the meetings were held with representatives of the microfinance sector and international financial donor organizations supporting the development of microfinance in Kyrgyzstan. Moreover, in order to identify in depth the problems and the factors hindering the effective development of microfinance in the Kyrgyz Republic, three regional “round tables” were conducted with the participation of microfinance sector representatives, where participants shared their views about the microfinance market and existing restrictions for its further expansion. This allowed the direct participation of the microfinance sector in the drafting of the Strategy, as well as the identification of its role in its implementation and attainment of objectives set.

Representatives of appropriate public institutions, MFIs, international donor organizations and companies that provide supporting services (consulting, information, training and personnel training) participated in developing a draft Strategy.

In the process of drafting a Strategy, the analysis of the microfinance sector has been conducted as well as the analysis of the normative and legal base regulating activities of institutions rendering microfinance services in Kyrgyzstan. The results of the analysis are given in the annexes to the Strategy. They served as a basis for the analysis of strengths, weaknesses, opportunities and threats (SWOT analysis) that is given in the body of the document.

2. Environment

2.1 Social and Economic Situation

At the beginning of the 1990's, Kyrgyzstan as well as other CIS countries entered the transition period that was accompanied by complex social and economic processes, including crises in the economy. Initiated economic reforms permitted to build the basis of the market economy.

For the past years the Kyrgyz Republic has been successful in achieving macroeconomic stability, poverty reduction and realization of institutional reforms. According to the data of the National Statistics Committee of the Kyrgyz Republic, the poverty level calculated by consumer expenditures on the basis of sample integrated research made up 45.9 percent in 2004.

Favorable foreign economic situation has positive effect on the expansion of external demand as a factor of economic growth, increase of population' income and promotion of business activities. During recent years the foreign trade is developed under conditions of a stable exchange rate. In 2004, the dollar exchange rate appreciated by 5.8% and made up 41.62 soms as of 2004 year-end. After a crisis in 1998, the financial sector of the republic entered into the phase of dynamic development.

The distinctive feature of recent years is the emergence and strengthening of MFIs in the financial market of Kyrgyzstan that have occupied free niches in the sphere of financial services, primarily, in the area of rendering financial services to the poor in the most remote regions of the republic.

2.2 Microfinance and National Programs

Several years ago, the development of microfinance became part of the national program of the Kyrgyz Republic¹, one of the goals of which is defined as follows: "... taking into account the fact that the income from self-employment (individual activity) is the basic source of income, especially, for the poorest population, large scale political activities will be conducted to develop private entrepreneurship among the poor population through the development and expansion of micro credit facilities. The Government of the Kyrgyz Republic will undertake measures that will promote the development of credit unions, credit cooperatives and similar institutions, as well as training mechanisms for them..."

There is current opinion that the expansion of financial services outreach for the population is one of key factors for further economic growth. The Agrarian Policy Concept of the Kyrgyz Republic until 2010, approved by the Resolution of the Government of the Kyrgyz Republic # 465 of June 22, 2004 "On measures for implementing the Decree of the President of the Kyrgyz Republic "On new directions and measures of land and agrarian reform" UP #142 of April 17, 2004, notes that "... rural crediting shall play an important role in increasing the efficiency of agriculture and decreasing of poverty level in rural areas...". The private financial sector will play a main role in reducing the poverty level. From this perspective, it is essential to increase the volume of financial operations. It is important to develop mortgage lending and financial leasing. Further development of the land market will lead to the fact that the land will become the basic pledge for credit recipients² in rural areas.

The leadership of the Kyrgyz Republic considers the promotion of microfinance development as one of priority objectives and views the microfinance sector as the main instrument for achieving top priorities of the public policy: poverty reduction and creation of additional work places.

3. Overview of the Microfinance Sector

3.1. History of Development

¹ Government of the Kyrgyz Republic: National Poverty Reduction Strategy, 2000.

² Annex 5.1. to the document Agricultural Policy Update, Kyrgyz Republic, November 2004

The microfinance sector in Kyrgyzstan is dynamically developing and is characterized by a wide variety of participants. The first microfinance organizations (hereinafter referred to as MFIs) emerged with the support of international donors. FINCA was the first to commence its operations in 1995. In 1997 KAFC was established and CUs commenced their operations.

Donors that invested more than 85 million US dollars³ in the microfinance sector have played a major role in its formation. The greater portion of funds was provided in the form of grants and loans to MFIs and CBs, and the portion of their funds were extended in the form of technical assistance, including training. Major donors include ADB, EBRD, GTZ, SECO, USAID, WB, TACIS, Central Asian American Entrepreneurship Fund, Mercy Corps, ACDI/VOCA and several NGOs. More detailed information on the donor support is given in Annex 5.

Apart from assistance in organizing MFIs, international donor support permitted to create mechanisms of the so-called wholesale lending. FCSDCU was established in order to support and extend wholesale loans to CUs. KAFC, being a state owned non-bank financial and credit institution and specialized in rural finance, also extends loans to some MFIs. In 2004, MCC “Frontiers” started its operations as a supplier of wholesale loans with support from the USAID.

Small MFOs, having small staff and less than 100 borrowers, operate in the market alongside large MFOs like FINCA with more than 20 thousand borrowers. There are also more than 300 CUs operating in the country. Since 2000, some CBs of the Kyrgyz Republic participate in the EBRD MSFF and rapidly build up their loan portfolio.

Thus, the microfinance market is not clearly segmented from the rest of the financial market. Although there is a common understanding about the type of clients - consumers of microfinance services, there are no specific providers of these services that monopolize this market. Typical MFIs like Financial Foundation MCA “Bai Tushum” issue loans up to 600 thousand soms⁴ while 5 CBs participating in EBRD MSFF extend loans with the minimum amount of 50 US dollars⁵.

Over ten years of the development, the microfinance sector achieved significant success. Kyrgyzstan is the first country in Central Asia where both the Law “On Microfinance Organizations in the Kyrgyz Republic” and the Law “On Credit Unions” have been adopted. This demonstrates significance that the state attaches to the development of the microfinance sector. The microfinance market of Kyrgyzstan is characterized by a wide diversity of participants engaged in microfinance from SHGs to CBs. The Government of the Kyrgyz Republic, the National Bank of the Kyrgyz Republic and international donors actively support the development of this sector.

3.2. General Information on the Sector

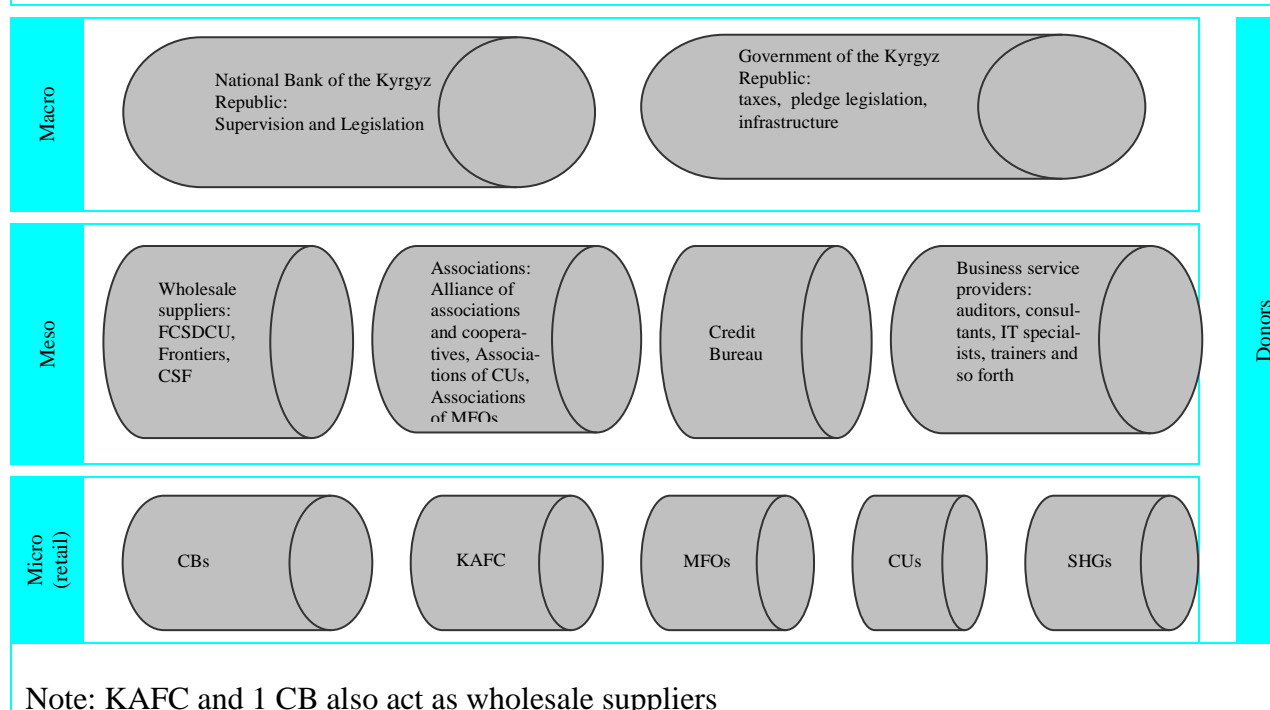
The microfinance system in the Kyrgyz Republic includes participants on three levels: macro, meso and micro. Major active participants of the microfinance sector are presented in the following scheme.

³ As of January 1, 2005, the equivalent in soms is 3.5 billion soms.

⁴ As of January 1, 2005, the equivalent in dollars is 14.6 thousand US dollars.

⁵ As of January 1, 2005, the equivalent in soms is 2.1 thousand soms.

Parties operating in the microfinance sector of the Kyrgyz Republic in 2005



As of January 1, 2005, the system of non-banking finance and credit institutions (hereinafter referred to as NFCIs) consisted of:

- 2 specialized finance and credit institutions – KAFC and FCSDCU;
- 78 MCAs and 26 MCCs known as forms of microfinance organizations;
- 305 CUs
- 116 pawnshops.

Moreover, as it has been already mentioned, 5 CBs are lending within the framework of the EBRD MSFF. Apart from that, approximately 1,256 SHGs provide basic financial services to their members.

As of beginning of 2005, the total number of borrowers of MFIs amounted to more than 100 thousand clients with an outstanding portfolio of 3,2 billion soms. The average loan size ranges from 18,7 thousand soms to 54,1 thousand soms depending on the type of institutions and target clientele. SHGs issue loans in the range of 2 thousand soms to 8,2 thousand soms.

Volumes of lending by microfinance sector participants (as of January 1, 2005)

Institutions	Number of institutions	Active portfolio		Number of borrowers	Average loan amount (US dollars)
		Million soms	Thousand US dollars		
KAFC	1	1,528	37,268	30,146	1,236
MCAs/MCCs	104	785	19,146	42,000	456
CUs	305	449	10,951	21,650	506
CBs in MSFF	5	463	11,293	8,707	1,297
Total	415	3,225	78,659	102,241	769

Source: analysis performed by the National Bank of the Kyrgyz Republic; US\$ 1 = 41 soms

3.3. Analysis of the Regulatory Environment⁶

3.3.1 STRENGTHS

Legislative framework

The legal environment has been created in the country without any serious restrictions for MFOs, CUs, KAFC and CBs to render microfinance services. The Law of the Kyrgyz Republic “On Microfinance Organizations in the Kyrgyz Republic” defines the possibility for the transformation of MFOs and CUs to deposit taking MFCs, and as a result of this come under prudential supervision of the National Bank of the Kyrgyz Republic. Financial and credit institutions independently set the rates of interest and commission fees.

Supervision

In the National Bank of the Kyrgyz Republic, NBSD supervises KAFC, FCSDCU, MFOs, CUs and other NFCIs. NBSD employees have been trained on the issues of practices, methodology and supervision. Manuals and internal supervision procedures have been developed for the purposes of proper performance of supervisory functions and trainings.

3.3.2 WEAKNESSES

Legislative framework

Normatives established for banks, KAFC and MFCs do not differentiate between microfinance and traditional lending. For example, with regard to the requirements related to the creation of the allowance for loan losses (hereinafter referred to as ALL).

In accordance with the Law of the Kyrgyz Republic “On Microfinance Organizations in the Kyrgyz Republic” MFCs can only perform micro credit, leasing and factoring operations, and attract time deposits. Meanwhile, clients of MFOs are also in need of money transfer services, and MFCs are in the position to render these types of services.

For this purpose the Law of the Kyrgyz Republic “On Credit Unions” needs to be amended in order to bring it into line with other legislative acts of the Kyrgyz Republic⁷. Major issues that need clarifications and/or decisions are, in particular, the following: the strengthening of corporate governance system; the improvement of the membership mechanism and the rules of general assemblies in terms of decision making procedures, the holding of repeated meetings, the introduction of the instrument of authorized representation of interests for participants of CUs; the remuneration to members of management bodies; authorities and responsibilities of all management bodies, in particular of the credit committee.

The Tax Code of the Kyrgyz Republic has rules that lead to the increased cost of micro creditting and unequal approach with respect to certain types of micro credit service providers, in particular, on the issues related to the deduction of expenses for ALLL creation from the taxable base of MCAs and MCCs that have the certificate of registration from the National Bank of the Kyrgyz Republic.

⁶ A detailed analysis of the normative and legal base is given in Annex 3 of this Strategy.

⁷ In particular, the Labor Code of the Kyrgyz Republic, the Civil Code of the Kyrgyz Republic and the Law of the Kyrgyz Republic «On Cooperatives».

Supervision

A large number and variety of MFIs create a problem for the National Bank of the Kyrgyz Republic to ensure proper supervision over their activities. Although prudential supervision is only exercised with respect to deposit taking MFCs, as well as CUs and specialized financial and credit institutions (KAFC and FCSDCU), the NBSD also performs the functions on licensing/issuing registration certificates and monitoring activities of all types of MFIs, irrespective of their size.

In July 2005, supervision functions over CUs have been transferred from FCSDCU to the National Bank of the Kyrgyz Republic. Currently the NBSD recruits appropriate inspectors and defines systems and procedures of supervision over CUs. The development of the appropriate supervision system has not been completed.

Collateral registration and impressment

Under the new Law of the Kyrgyz Republic “On Pledge” adopted in 2005, a process of collateral registration and a procedure of collateral impressment have been simplified. Nevertheless, some problems remain.

3.3.3 OPPORTUNITIES

Legislative framework

In order to attract additional resources for microfinance, the Law of the Kyrgyz Republic “On Microfinance Organizations in the Kyrgyz Republic” specifies the right for a MFC to obtain a license for attracting time deposits. Other options for increasing the resource base include strategic alliances of MFOs with CBs⁸, lending from commercial wholesalers or from international donors, as well as from social investors.

Currently, only three MFOs are interested in attracting deposits and transforming into a MFC or a bank. During the next two years, the National Bank of the Kyrgyz Republic can introduce required amendments to the microfinance legislation by relying on the experience gained in reorganizing these financial institutions. These amendments will be primarily directed to balance between the pursuit to reduce risks of the financial system and NFCIs in order to protect interests of depositors and other creditors, to build adequate supervision and provide a wider access for MFIs to performing deposit transactions. An authorization to attract deposits from the public will be exclusively granted to institutions demonstrating financial sustainability and not posing destabilization risks for the banking system, violation of its safety and soundness.

CUs have substantially improved their organization level and now represent their common interests through established associations. The dialogue with the National Bank of the Kyrgyz Republic on regulation and supervision issues has become more intensive, and currently CUs prepare proposals to introduce changes to the Law of the KR “On Credit Unions”.

Supervision

It is expected that during the forthcoming two years, the first MCAs and MCCs will be transformed into MFCs. Correspondingly, the National Bank of the Kyrgyz Republic has the op-

⁸ Strong links with banks permit MFOs to use their comparative advantages, for example, such as the establishing of close contacts and knowledge of clients, special methods and technologies for delivering credit services to the poor. Comparative advantages of banks include the access to large funding sources and availability of diversified financial products, such as various types of deposits, payment transactions and transfers.

portunity to increase its own supervisory capacity during this period and develop required normative documents.

The analysis based on early warning system can become one of basic blocks for the supervisory system of CUs.

Collateral registration and impressment

The Council of banks established a working group on the development of necessary changes to the legislation of the Kyrgyz Republic in order to solve problem issues related to collateral registration and impressment. USAID legislation improvement project conducted a review and a study to identify problems and to prepare necessary changes to the legislative acts of the KR on pledge issues. In addition, within the framework of Interdepartmental Commission on the inventory of normative acts of the Kyrgyz Republic, there are activities in progress on introducing amendments and addenda to the Civil Code of the Kyrgyz Republic and to the Land Code of the Kyrgyz Republic in order to eliminate inconsistencies with the Law of the Kyrgyz Republic “On Pledge”.

3.3.4 THREATS

Legislative framework

Risk of reputation and image of MFOs: since MCAs and MCCs are sufficiently easy to establish due to their organizational and legal form, people wanting to engage in this activity can easily register an appropriate form of the organization and apply to the National Bank of the Kyrgyz Republic for a certificate of registration. This does not necessarily mean that they will actually engage in micro crediting. This partly explains the fact that currently almost 40% of registered MCAs do not operate. Thus, in practice a large number of MCAs and MCCs are weak, inefficient, and are a burden for the National Bank of the Kyrgyz Republic regulating their operations.

Presently, the legislation of the Kyrgyz Republic has certain deficiencies for smooth transformation of financial and credit institutions into MFCs⁹.

Delay in the adoption of a draft new Tax Code of the Kyrgyz Republic concerns microfinance market participants by the fact that many taxation issues that must be solved in the new draft law will not be adopted.

Currently a draft law “On Credit Bureau” is being developed. Too much control and restrictions can impede their development.

Supervision

Insufficient differentiation of regulatory requirements for microfinance and traditional bank lending can hamper the growing involvement of CBs in the delivery of micro credit services.

3.4 Analysis of the Microfinance Sector¹⁰

3.4.1 STRENGTHS

⁹ These procedures are established by various legislative acts: the Civil Code of the Kyrgyz Republic, the Law of the Kyrgyz Republic « On Microfinance Organizations in the Kyrgyz Republic», the Tax Code of the Kyrgyz Republic, Interim Rules for Regulating Operations of Microfinance Companies on the Territory of the Kyrgyz Republic (approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic #4/2 of February 19, 2003, registered by the Ministry of Justice of the Kyrgyz Republic #29-03 of March 25, 2003), procedures for notarial registration and registration of new legal entities.

¹⁰ A detailed analysis of the microfinance sector is included in Annex 2 of this Strategy.

In comparison with other Central Asian countries, the microfinance sector in the Kyrgyz Republic has the most advanced and diversified network of NFCIs.

CBs entered the microfinance market by implementing EBRD MSFF. Within the framework of EBRD MSFF a specialized efficient lending technology has been introduced in five banks that resulted in the rapid growth of their clientele.

The presence of various types of micro credit providers can be considered as an advantage. It contributes to a diversified supply of financial services and in general generates the necessary competition.

On the entire republic scale a wide retail micro credit network has been established: altogether NFCIs and banks have more than 570 offices placing micro credits.

K AFC is one of the largest specialized rural finance and credit institution in Central Asia serving 30 thousand clients through its countrywide network of 11 branches and 47 representations.

The strength of CUs is their pursuit to improve their position by combining efforts in order to facilitate independent economic activity that is based on self-help, self-management and sense of own responsibility. In addition, the location of CUs is, in principle, their strength, as in most cases CUs had been set up in rayons where there were no other financial institutions. Some of them have taken such advantage, however by the beginning of 2005 only 91 out of 305 credit unions had more than 100 clients, and none had more than 1000 clients.

In the market segment offering services to the poor: the UNDP sponsored program has been promoting the creation of SHGs (informal community based organizations at the village level). By the end of 2004 there were 1256 SHGs that received financial resources from K AFC for on-lending among their members.

In the country there is a credit bureau that has information about borrowers which is obtained from most banks and bigger MFOs.

New whole sale lenders (LLC MCC “Frontiers” and CSF) started to fund well-managed and effectively performing MFOs and CUs.

International donors¹¹ take an active part in the development of the microfinance sector in the Kyrgyz Republic.

3.4.2 WEAKNESSES

A wide and diverse network of microfinance providers has led to the market fragmentation with the characteristic presence of a great number of small micro credit providers. As of beginning of 2005 only 5 MFIs had more than 1000 clients. 12 MFOs had between 100 and 1000 borrowers, while 87 MFOs had less than 100 clients or they were not operating at all. Since the scale is very important for sustainable provision of microfinance services, most of small organizations have not performed active operations. In view of such small size of MFOs only relatively high interest rates of loans and low cost of financial resources permitted them to survive.

In spite of the high number of micro credit providers, the provision of financial services to the poorer households, small farmers and people living in remote areas is considered to be insufficient.

Due to lack of information it is difficult to determine the impact that the micro credit has on economic and social condition in the country.

¹¹ See a detailed analysis in Annex 5 to this Strategy.

Funding problems

Most MFOs have small capital. CUs have limited possibilities to increase their equity and attract external borrowings. Consequently, they have limited funds that can be used for lending. Traditionally the sector depended on donor money and until now external borrowings from donors are considered to be one of major funding sources for lending operations of CUs.

Local alternative sources of funding for the micro credit sector as such are not sufficiently developed to fill the gap left as a result of donor support cut down.

Most MFOs and CUs have an inadequately developed institutional set up that is characterized by a weak governance structure and a low level of managers qualification that frequently have no suitable educational background in the area of finance or management. There is lack of staff, in particular, personnel with knowledge and skills of lending, accounting and management information systems. Applicable systems (lending methodology, risk analysis, management information systems) are poorly developed.

KAFC's portfolio is characterized by low sectoral diversification and is practically represented by 100 percent loans to rural sector, mainly for livestock. KAFC is substantially dependent on credit lines from foreign sources.

According to international standards defined by the MIX Market organization, very few micro credit providers extend loans with an average loan size within the category of loans "for the very poor"¹². One medium size MCC, LLC MCC "Kyrgyz Ayltrust" provides loans with an average size of 2 thousand soms that closely fits the category of loans "for the very poor". On average, MCAs, MCCs and CUs extend loans with an average size corresponding to average indicators on the category of loans to the "poor households". The average size of loans issued by KAFC indicates that their customers are not small (smallest) farmers.

Most participants of the microfinance sector, including KAFC and CUs do not present information to the Credit Bureau as most small MFIs can not afford its services in view of their relatively high cost.

Provision of regular training to MFIs and their personnel (by training centers, consultants) is very limited. The use of specialized advisory services is practically non-existent.

Although there is understanding among MFIs concerning the need for training, this does not yield in any visible and real demand on their part, willingness to pay for such training as most MFIs do not provide expenses for these purposes.

3.4.3 OPPORTUNITIES

Although there is no countrywide study there is a current opinion that there is large pent-up demand for credit. In order to respond to this demand, particularly, in rural areas with low client density and small loan amounts, financial institutions should operate with higher efficiency; they require on-going training, technical assistance and access to technologies for improving their efficiency.

With more than 100 thousand borrowers of MFIs as of beginning of 2005 and 5,1 million population, the microfinance services cover 2 percent of the population: out of every 100 inhabitants, only two have access to a micro credit¹³. This is considered to be a high indicator¹⁴

¹² Four categories as defined by the MIX Market: the very poor households: average loan size is less than 20 percent of GDP per capita; poor households: 21-150 percent; average households: 151-250 percent; small business: more than 250 percent.

¹³ For example, in Bangladesh, the outreach indicator is at the level of over 8 percent of the population, while in Bolivia it is almost 6 percent.

as compared with other Central Asian countries. Meanwhile, it is low in comparison with countries with a long microfinance history that indicates the growth potential.

As the economy develops, there will be an increasing demand for a diverse range of credit products (leasing, consumer lending, medium term lending) and other financial products (national and international money transfers, various types of deposit products, insurance services).

The necessary growth of MFOs can be ensured by the strategy for their merger. Mergers based on joint objectives can expand the geographical coverage and clientele base, facilitate the increase of cash flows and access to capital, and achieve economies of scale in view of reducing fixed costs¹⁵.

In spite of doubts concerning the saving capacity of the population, some NFCIs take steps to transform into deposit taking institutions in order to fund their further growth and reduce donor dependence. In-depth studies of market demand for savings to confirm this growth opportunity were not performed¹⁶.

CUs, in view of their location, have good opportunities to mobilize public savings. In 2004 a pilot project was implemented within the framework of which 10 selected CUs mobilized savings of their participants totaling to 2,5 million soms. This pilot project was implemented by the National Bank of the Kyrgyz Republic with the technical assistance from GTZ project.

SSC can play an important role in the microfinance sector: part of its deposits can be targeted for providing financial resources to MFOs and CUs (a function of a whole sale lender). It can provide payment and other monetary services to these institutions through its countrywide network.

There are opportunities for the operation of one or more microfinance associations in the areas of information gathering and exchange, lobbying of common interests, institutional capacity building of the sector, in particular, by developing procedures and operations standards for their members.

There are opportunities available for training in lyceums of cities of Bishkek and Osh where educational courses for training junior bank employees have been opened with the support of GTZ project. CUs and other MFOs can use these training programs.

The Microfinance Center for Eastern Europe and CIS that is based in Poland has recently established a training center in Almaty to conduct short-term courses for Central Asian countries. This is expected to increase the training opportunities for MFIs.

Several donors (GTZ, WB, USAID, EBRD, UNDP, Soros Foundation-Kyrgyzstan) are interested to continue supporting the development of the microfinance sector. Donors can set up or provide funding for setting up institutional support mechanisms for MFIs (training institutions, required equipment, training manuals and so forth), and support the research and introduction of best practices on solving such important problems as, rural finance and new product development. They can also fund the market and impact research.

¹⁴ There are essential distinctions in the microfinance outreach by oblasts with the highest outreach indicators in Issyk-Kul Oblast (3.9 percent) and Talas Oblast (3.5 percent).

¹⁵ Merger examples in the country. MCA "Bai Tushum" was established in 2000 by merging ACDI/VOCA and Caritas programs. In 2005 three microfinance institutions supported by Mercy Corps joined and formed a MCC "Financial group kompanion".

¹⁶ It is planned to privatize and transform KAFC into a commercial bank. Two MFOs, MCC "FINCA" and MCA "Bai Tushum" plan to be transformed into MFCs. MCC "Financial group kompanion" considers the possibility of becoming a bank.

3.4.4 THREATS

Provision by some MFIs established by government institutions of micro credits at subsidized interest rates that is lower than the market rates reduces the possibility for the development of the sector.

Volumes of donor grant support for lending reduce, at the same time there are no alternative (commercial or semi-commercial) sources that can be immediately used to respond to the large unmet demand.

The lack of adequate secondary institutions¹⁷ and systems for CUs (apex institution, payment system, independent audit) is a threat for their future development.

4. Strategy

Currently one of the main strategic objectives of the Kyrgyz Republic is to improve living standards of the population. According to official figures a significant portion (more than 45 percent) of the population lives below the poverty line.

One of poverty alleviation methods is to create conditions for the development of entrepreneurship. The majority of people with low income can not afford traditional sources of funding for developing their businesses. The development of MFIs is the way out of this situation. The main objective of the micro credit development process is to render assistance to the poor by transforming lending into a more efficient instrument supporting the poverty reduction strategy that is developed and implemented in the republic. The National Bank of the Kyrgyz Republic makes a significant contribution to the creation of conditions that facilitate the development and the strengthening of microfinance in the Kyrgyz Republic. Such initiative sets a feasibly attainable objective – to scale up operations and to increase volumes of services in order for the microfinance to become a sustainable component of the country's financial system in general.

Besides, it is expected that the growth of the microfinance share will have favorable impact on the investment lending of the republic.

4.1. Integrity of the Microfinance Strategy

The microfinance development strategy in the Kyrgyz Republic is aimed at further development of the integral financial system that works for the majority.¹⁸

In order to achieve the stated objective it is necessary to consolidate efforts of interested parties at different levels: the Government of the Kyrgyz Republic and the National Bank of the Kyrgyz Republic, financial and credit institutions, including banks and a non-governmental sector that provides supporting services for the microfinance sector, as well as the donor support is required. The Strategy is an integral document and is aimed at providing access to financial resources for wide segments of the population of the republic: from the poorest households and small farmers to city dwellers and micro enterprises.

The Strategy gives an integral presentation of the future development of microfinance in the country, describes major rules and laws of operation that must facilitate the exchange of information and involvement of a greater number of participants in this process. It is also inclusive because it considers microfinance as part of the country's financial market with which

¹⁷A detailed analysis is in Annex 4 to this Strategy.

¹⁸ The term «Financial systems that work for the majority» was introduced by Women's World Banking in 1995.

the integration is steadily increasing: microfinance institutions intend to gradually increase the scale of their operations.

Microfinance is aimed at providing equal access to financial resources for the public residing in remote rayons of the republic and its development must be ensured at three levels:

- 1) “Micro level” – a wide range of financial institutions that are encouraged to serve the needs of the poor, micro entrepreneurs, small farmers and other economic entities;
- 2) “Meso level” - audit organizations, rating agencies, associations, credit bureaus, transfer and payment systems, information technologies, technical service providers, advisory services and training programs;
- 3) “Macro level” – the National Bank of the Kyrgyz Republic, the Ministry of Economics and Finance of the Kyrgyz Republic and other public institutions ensuring legal status (“rules of the game”) for participants of the microfinance sector.

The integrity of the Strategy in its turn predetermines that the implementation of the Strategy is the objective for all parties participating in the microfinance process.

All interested parties are encouraged to contribute to the attainment of a common objective: ensure access to sustainable financial services for wide segments of the population of the Kyrgyz Republic.

In the process of achieving this goal, participants will be free in making their own strategic choice. The Strategy clearly determines the future development thus permitting participants to make more efficient decisions. This Strategy facilitates the development of the business environment, encourages cooperation, information exchange and expression of common vision, in particular, on the achievement of consensus on legal issues.

The need for integration and recognition of the microfinance by the state as an individual segment of the financial sector, the development of which is required not only to support small entrepreneurship, but mainly to improve the public access to financial resources.

Success in attaining goals and objectives of the Strategy is determined by the integrity of financial systems, by the integration of financial services of the microfinance sector into the financial market and the efficiency of interaction among all microfinance levels. In addition, financial systems for the poor depend on existing conditions, such as infrastructure, access to markets, production technology and availability of information to mitigate risks.

Support of international organizations is one of important and positive factors as donors provide funding for setting up institutional support mechanisms for MFIs (training institutions, necessary equipment, training manuals and so forth), support the introduction of best practices in the area of rural finance and new product development (savings products, micro insurance, money transfers, leasing), as well as collaboration between MFIs and banks.

International organizations also play a certain role in the microfinance market. Currently, an increasing number of specialized international microfinance funds offer different types of financial products for MFIs: subordinated loans, guarantee funds and so forth.

4.2 Goals and Objectives of the Strategy

The main goal of the Strategy is to reduce poverty by expanding access to financial services for poor segments of the population in remote regions of the Kyrgyz Republic. Implementation of the goal of the Strategy will result in the creation of the microfinance market infrastructure and new jobs in the near-term.

Objectives of the Strategy are as follows:

- Develop strategic lines of the microfinance sector development in the Kyrgyz Republic for 2006-2010;
- Coordinate activities of public bodies on developing mechanisms and solving problem issues hampering the development of microfinance;
- Promote the expansion of microfinance services for the poorest sections of the population in remote regions of the country;
- Promote the institutional and financial strengthening of MFIs in order to increase their efficiency;
- Diversify microfinance services, in particular, savings services and remittances;
- Facilitate the increase of loans funded from internal sources, in particular, public savings and commercial sources of funding;
- Stimulate the development of supporting services and infrastructure that provides access for MFIs to professional services and information.

4.3 Strategic Lines

In order to implement the stated objectives, the Strategy stipulates the following:

- Improvement of the legal environment: further improvement of the regulation that meets the development conditions of the microfinance sector, including encouraging a diversity of MFIs. Emphasis shall be made on the development of private microfinance structures and reduction in the share of MFOs funded by the state;
- Integration of the microfinance sector into the country's financial system, in the first place, by the scale up of MFIs operations, integration and strategic alliances between individual NFCIs;
- Provision of microfinance and other financial services to the public in remote regions of the country (geographical expansion in covering the public). Encourage improvement of efficiency and competitive advantages of MFIs that render services to micro enterprises, small farmers and poor households;
- Development of the microfinance service sector and its diversification;
- Improvement of the role of funding the microfinance from internal sources. Transition of the donor support from direct microcredit funding to improving the institutional capacity of microfinance providers. Donor funds for on-lending will be provided to MFIs through wholesale lending mechanisms. The role of funding the microfinance from internal sources and using commercial loans from domestic and international organizations will be improved on the condition of availability of transparent information on operations of MFIs;
- Creation of the services market for the microfinance sector in the areas of training, consulting, accounting, audit and management information systems;
- Strengthening of the meso structure for the microfinance sector, including associations of MFIs and credit bureaus;
- Coordination of donors supporting the microfinance sector.

5. Anticipated Results and Indicators

Subject to realization of the action plan over the next five years, it is anticipated that the Strategy will contribute to the achievement of the following results:

- 1) Expansion of the outreach that includes:
 - Population coverage by microcredit will increase from 2 to 4 percent. Active borrowers will approximately make up 220 thousand persons;

- Total loan portfolio of financial institutions providing microfinance services will amount between 6 billion soms and 7 billion soms;
- 2) Expansion of funding by mobilizing 3 to 4 billion soms to fund the growth of the microfinance portfolio. These funds will come from different sources: from international social investors and microfinance funds, commercial wholesale lenders, equity of NFCIs, private savings and deposits;
- 3) Improvement of legislative and regulatory framework that includes the provision of adequate legal environment by:
 - a) considering the possibility to introduce amendments to the following laws of the Kyrgyz Republic:
 - «On Microfinance Organizations in the Kyrgyz Republic» by the end of 2008;
 - «On Credit Unions» by the end of 2006;
 - Tax Code of the Kyrgyz Republic with regard to providing tax benefits for deducting ALL expenses from a taxable base and removal of tax on interest income for wholesale lenders by the end of 2006;
 - b) developing regulatory and supervisory structure for NFCIs. The National Bank of the Kyrgyz Republic emphasizes the prudential supervision of deposit taking institutions. At the same time, prudential supervision will be exercised with respect to NFCIs that have significant impact on the financial and credit sector resulting from the large volume of active operations or the presence of structural interrelations with other financial institutions;
- 4) Development of supporting services and meso infrastructure, including:
 - Development of the market of supporting services (training, technical assistance, accounting and audit) for the microfinance sector;
 - Establishment of an appropriate APEX structure for CUs;
 - Activization of operations of credit bureaus so that they hold information about more than 70 percent of microfinance sector clients;
 - Development of financially sustainable wholesale lenders.

6. Strategy Implementation and Monitoring Process

The implementation of the Strategy depends on the interest and the capacity of all institutional participants of the microfinance market to carry out actions, activities and recommendations defined in the Strategy. The ways of attaining objectives of the Strategy are specified in the attached action matrix (action plan).

6.1 Role of Major Participants

This section defines the role of each party. The action matrix (action plan) contains more detailed information about the role and the contribution of each party in solving problems and achieving specific objectives.

6.1.1. Government of the Kyrgyz Republic, National Bank of the Kyrgyz Republic and other public bodies shall ensure the following:

- An appropriate legal and regulatory environment, including the introduction of appropriate amendments to the Laws of the KR “On Credit Unions” and “On Microfinance Organizations in the Kyrgyz Republic”;

- Prudential supervision only with respect to NFCIs that accept deposits, as well as with respect to NFCIs (based on exceptions) that have significant impact on the financial and credit sector resulting from the large volume of active operations or the presence of structural interrelations with other financial institutions;
- Fulfillment of appropriate actions that are required from public organizations in accordance with the action matrix that includes the introduction of amendments to the Tax Code of the Kyrgyz Republic with regard to the settlement of taxation issues for financial intermediaries and other;
- Orientation of donors towards the provision of wholesale microfinance mechanisms, support for the meso structure and the institutional sustainability of MFIs;
- Gradual reduction of the government participation in the microfinance market through various projects (programs) and institutions subsidized by the government;
- Assistance to microfinance institutions in solving priority social objectives on poverty reduction and creation of jobs.

6.1.2 Microfinance institutions shall ensure the following:

- Expand operations, ensure sustainable development and increase the coverage of the country's population with financial services;
- Diversify and improve financial services in line with the demand of the population;
- Promote the creation of microfinance associations and improve the capacity of the sector in protecting its own interests;
- Gradually diversify the sources of microfinance funding that will contribute to the reduction of donor assistance dependence;
- Formulate proposals for obtaining technical donor assistance in such a manner that this assistance is targeted at the institutional development of MFIs;
- Refrain from the offer of subsidized financial services.

6.1.3 Meso level organizations will encourage the following:

- Strengthening of the role of associations in the microfinance sector. Objectives of associations are as follows: collection and exchange of information; providing access for MFIs to the best international microfinance practices; representation and lobbying of sector interests; analysis of the legislative framework regulating activities of MFIs and elaboration of proposals for its improvement; provision of consulting services; organization of training courses; contribution to the strengthening of the institutional capacity, sustainability and professional reputation by introducing stricter performance standards, particularly, in the governance system and transparency;
- Growth of the sector through the development of credit bureaus that will gradually expand their institutional and geographical coverage;
- Development of wholesale funding institutions for MFIs that will contribute to the growth of the microcredit portfolio and will encourage a closer link of sector participants with national and international financial markets.

6.1.4 The following is expected from donors:

- Continue supporting the microfinance sector on CGAP principles;
- Continue the dialogue and the exchange of information in the area of transfer of international experience;
- Support government and private structures in orienting their activities in the microfinance sector towards the achievement of the Millennium Development Goals.

6.2. Microcredit Funding Sources

Microcredit funding sources are as follows:

- National wholesale lenders attracting international and domestic resources for on-lending to MFOs and CUs;
- SSC that has the capacity to participate in the microfinance market as a wholesale lender using the portion of its deposit base;
- CBs that target the portion of their deposits to the microfinance market;
- International social investors and microfinance foundations that fund wholesale lenders and some NFCIs by providing, in particular, subordinated loans for their capital and guarantee funds;
- Savings of the public in the form of savings shares and deposits in CUs from participants, as well as deposits of MFCs.

6.3 Monitoring Strategy Implementation

The Strategy is designed to define the development directions for the microfinance sector of the Kyrgyz Republic for 2006-2010. The implementation of this Strategy will be monitored at two levels: the achievement of results as mentioned in chapter 5 and the fulfillment of measures and actions as defined in the Action Matrix (action plan). A working group comprising of representatives from all microfinance sector participants will monitor the implementation of the Strategy.

7. Action Matrix (Action Plan)¹⁹

The Action Matrix includes specific activities that are grouped by the following sections:

7.1. Activities on Improving Legal and Regulatory Microfinance Environment

7.1.1 Activities on improving the legal framework regulating operations of MFOs, include the following:

- 1) Detection of inconsistencies in the Law of the Kyrgyz Republic “On Microfinance Organizations in the Kyrgyz Republic” (from 2006 to 2007) with other legislative acts of the Kyrgyz Republic, as well as detection of other deficiencies that hinder the enhancement of efficiency in operations of MFOs;
- 2) Preparation of the draft law on introducing amendments and addenda to the Law of the Kyrgyz Republic “On Microfinance Organizations in the Kyrgyz Republic” and its adoption before the end of 2008;
- 3) Research problems of transformation of MCAs and MCCs into MFCs, in this case it is necessary to:
 - Consider the possibility of setting in normative and legal acts of the National Bank of the Kyrgyz Republic a three year period to bring the ownership structure of a MFC into line with the requirement of no more than 20 percent of ownership share of legal entities (these changes should not refer to a MFC intending to obtain or hold a license for deposit acceptance);
 - Consider the possibility to revise Attachment 1 of the Interim Regulation “On the Establishment of Microfinance Companies on the Territory of the Kyrgyz

¹⁹ Action plan for the implementation of the Medium Term Microfinance Development Strategy is given in Annex 1 of this Strategy.

Republic” currently in effect (approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic #42/1 of October 11, 2002, registered with the Ministry of Justice of the Kyrgyz Republic #143-02 of November 14, 2002) with regard to introducing addenda to the list of international organizations qualified to serve as the founders of MFCs without limiting their share interest;

- Consider the possibility to exempt MCAs and MCCs transforming into MFCs from the requirement of depositing the minimum amount of authorized capital in a bank account prior to obtaining a license. This requirement should only apply to newly established MFCs;
- Establish requirements to personnel qualification of an MFC, including the work experience both in the banking sector and in the microfinance sector.

7.1.2 Activities on improving the legal framework regulating activities of CBs stipulate the following:

the possibility to revise the Regulation “On Lending in Commercial Banks and Other Financial and Credit Institutions Licensed by the National Bank of the Kyrgyz Republic” (approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic #12/7 of April 27, 2005, registered with the Ministry of Justice of the Kyrgyz Republic #69-05 of June 3, 2005) with regard to the requirement on monitoring the pledge on a monthly basis.

7.1.3 Activities on improving the legal framework regulating activities of CUs include the following:

- 1) Bring the Law of the Kyrgyz Republic “On Credit Unions” into line with other laws of the Kyrgyz Republic by the end of 2006. It is expected to consider the following possible changes to the law:
 - concerning the membership for associated members;
 - on the introduction of corporate principles, including the improvement of procedures for conducting meetings of participants, determining the quorum of the general meeting of participants of CUs, imposition of responsibility for issued loans to the credit committee and determining remuneration for board members of CUs;
- 2) Revise the existing Regulation “On Licensing of Credit Unions” (approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic #14/3 of May 4, 2005, registered with the Ministry of Justice of the Kyrgyz Republic #75-05 of June 10, 2005) to the extent of possible introduction of amendments and addenda with respect to minimum requirements of the National Bank of the Kyrgyz Republic for obtaining a license entitling to attract deposits. These requirements must be considered in 2006;
- 3) Develop a multilevel system of regulating MFIs. In developing requirements provide for prudential supervision of deposit taking MFIs as well as with respect to MFIs (based on exceptions) that have significant impact on the financial and credit sector resulting from the large volume of active operations or the presence of structural interrelations with other financial institutions.

7.1.4 Activities on the simplification of pledge registration and impressment procedures provide for the following:

- 1) Reduction of transaction costs in registering movable and immovable property as pledge by considering the following possibilities:
 - Locate notary's offices, offices of the State Agency on Registration of Title to Real Property and the Central Pledge Registration Office in one building;
 - Introduce changes to certain legislative acts of the Kyrgyz Republic that involve the solution of the issue concerning the opening of representative offices of the State Registry in aiyl okmoty and entitling them to perform all functions on the registration and execution of the pledged property in order to reduce the costs of the rural population;
 - Simplify collateral registration procedures for repeat borrowers using the same collateral;
 - Revise annual certification requirements for the immovable property used as the pledge in obtaining loans;
- 2) Improvement of mechanisms on the sale of pledged land in order to use land as collateral in a more efficient manner, for example, appraisal procedures;
- 3) Amend legislation to determine sanctions when selling pledged movable property that has not been registered, and improve the procedure of extra judicial collateral impressment.

7.1.5 Activities on improvement of taxation in financial and credit institutions stipulate the following:

- Consider the possibility of tax exemption for expenses on establishing ALL for MCAs and MCCs that have the certificate of registration of the National Bank of the Kyrgyz Republic as in the case of financial and credit institutions that have the license of the National Bank of the Kyrgyz Republic;
- Streamline the taxation of interest income from leasing transactions within the framework of activities on the development of leasing in the Kyrgyz Republic.

7.2 Activities on Expanding Geographical Scope and Coverage of Poor Households with Microfinance Services

In order to expand geographical scope and cover poor households with microfinance services, it is necessary to:

- Study the demand for financial services among small farmers and rural households to further inform microfinance providers;
- For the purposes of further development of KAFC sustainability it is necessary to announce the bid for the sale of KAFC and complete the privatization of KAFC by the end of 2006. Within the framework of KAFC privatization process, it is necessary to consider the issue of transforming KAFC into a bank. Develop measures that will keep KAFC focused on rural finance after its final privatization;
- Assist self-help groups through which poor households obtain access to credit facilities.

7.3 Activities on Diversification of Microfinance Services and Capacity Building of Microfinance Providers

In order to diversify microfinance services it is necessary to:

- Improve the regulatory environment in order to diversify services rendered by MFIs;
- Encourage pilot projects with the involvement of financial institutions, trading and production cooperatives, suppliers of equipment and parts for introducing agriculture oriented financial products (for example, financing the construction of storages, provision of commodity loans);
- Assist in the development of new products of MFOs and CUs, or in the modification of existing ones oriented at meeting the needs of clients (micro leasing, micro insurance, mortgage loans), as well as support in obtaining innovation grants for the development of new products by rural MCAs and CUs working with poor households;
- Encourage professional and business contacts between CBs and NFCIs through their associations for exchange of technologies, strategic merger, wholesale lending of MFOs by banks and so forth.

In order to strengthen the capacity of MFIs it is necessary to:

- Increase the efficiency of MFOs, CUs and CBs in order to improve their cost structure allowing them to work in areas with low population density and provide small loans. This can be achieved by providing technical assistance, access to new lending technologies, improved risk management systems and loan tracking systems;
- Facilitate the access of MFOs, CUs and CBs to specialized technical assistance and training, as well as establish a structure supporting the microfinance sector that will be managed by an independent party and, mainly, operate at the expense of a co-financed fund. One of the functions of this structure is to provide specialized technical assistance and training;
- Conduct trainings not only at special courses but within MFIs. Other initiatives can include scholarships for the participation of microfinance practitioners in international training, for example, in the new training center of the Microfinance Center in Almaty and the participation in annual national conferences on microfinance to be organized with joint efforts of MFIs and donors;
- Facilitate the dissemination of more exacting performance standards in MFIs focusing special attention on governance issues;
- Establish a fund with donor support to conduct research in the area of strategic merger of banks and/or certain NFCIs.

7.4. Activities on Expanding Funding Sources of Microfinance Providers

Expansion of microfinance sources provides for:

- 1) Development of the national savings culture and fulfillment of a number of actions, including:
 - determine requirements set to CUs for obtaining a license authorizing to attract deposits from participants to enable CUs to mobilize savings;
 - provide detailed information about international experience on savings mobilization among poor households to interested MFOs and CUs (for example, Bangladesh, Bolivia);
- 2) Ensuring the transparency of the microfinance market and microfinance providers in order to attract domestic and international commercial loans. MCAs, MCCs and CUs must regularly publish their financial statements on a donor-supported Mix Mar-

- ket²⁰ electronic page that offers a free and easily accessible information service for practitioners and investors. Associations of MFOs and CUs must assist their members that have no possibilities to use Internet services. Deposit taking institutions shall provide information on the financial standing and portfolio condition certified by an independent audit;
- 3) Creation of mechanisms for obtaining commercial funding for MFIs, both on national and international levels. Possible mechanisms are as follows:
 - Capitalization of MFIs. Equity is considered as a condition for mobilizing loans from national and international sources and can be essential for the growth of small MFIs;
 - Partial loan guarantee schemes can facilitate the provision of credit lines for MFOs and CUs by banks.
 - 4) Study of the possibility to channel part of deposits of the Settlement and Savings Company to the microfinance sector by assigning SSC a wholesale lender function for NFCIs.
 - 5) Involvement of international social investors in the microfinance sector of Kyrgyzstan. Possible actions in this area are as follows:
 - Representation of the microfinance sector of Kyrgyzstan at the Annual CIS Investment Forum in Moscow and/or at annual international conferences organized by MFC for Eastern Europe and CIS;
 - Organization of regular conferences with donor participation;
 - Dissemination of the experience of interaction between social investors and MFIs of Kyrgyzstan.

7.5 Activities for Building the Market of Supporting Services and for Strengthening Microfinance Infrastructure

In order to build the market of supporting microfinance services it is essential to:

- Prepare a group of qualified microfinance consultants and trainers that can provide qualitative services to MFOs (on training of loan officers, managers, accountants and auditors);
- Improve qualification of accountants and auditors on an on-going basis;
- Develop a donor-supported project on information system enhancement for small MFOs, in particular, to automate accounting and improve loan portfolio management;
- Create with donor support a response system to requests of MFOs that are willing to acquire information systems, in particular, computer-based accounting programs. Attract consultants and conduct trainings in the area of information systems, including computer-based accounting programs.

In order to strengthen the microfinance infrastructure it is necessary to:

- Support the initiative to establish an Association of MFOs. Large MFOs will combine their efforts to prepare a business plan of the Association;

²⁰ See: www.mixmarket.org

- A microfinance resource center will be established within the Association to provide information on the best national and international practices, and information on funding sources;
- Ensure open membership in the Association for CUs and banks rendering microfinance services, and possibly assist in the establishment of an alternative Association for institutions subject to prudential supervision;
- CUs must create a well-functioning secondary structure (financial apex organizations and a Stabilization Fund) to support their operations. Provide for the possibility to privatize Financial Company for Support and Development of CUs taking into account the results of ADB technical mission;
- Continue expanding operations of credit bureaus, assist in the submission of information by all microfinance providers on a voluntary basis. The lack of communication facilities can be solved by providing access to Internet services for small MFIs. Internet connection can be used to provide financial information to the National Bank of the Kyrgyz Republic and to obtain international information on microfinance. A differentiated approach can be applied to small MFOs in setting prices for Internet services;
- Wholesale lending institutions must be developed as a source of resources for MFOs and CUs. The growth of existing wholesale lending institutions will be encouraged that should result in the growth of competition;
- In order to protect clients of MFIs, associations of MFIs must publish on a regular basis information on applicable interest rates on loans charged by participants and other useful information for clients.

7.6 Activities on Coordinating the Work of Donors Involved in the Microfinance Sector

Coordination of donors involved in the microfinance sector provides for the following:

- Active involvement of donors in implementing the microfinance strategy;
- Enhancement of the role of associations of MFIs in coordinating sector requests and attraction of donor assistance to meet them. It is essential that Associations of CUs develop a program supporting the development of CUs that will serve as the continuation of successful collaboration with GTZ technical assistance program;
- Coordinate donor programs taking into account actual needs of the microfinance sector in order to use donor assistance in an effective and optimal manner.

7.7 Strategy Monitoring Mechanism

A working group comprising of representatives of public bodies, associations of MFIs and international donor organizations will be established to monitor the implementation of the Strategy. Administration of the President of the Kyrgyz Republic will coordinate activities of the working group.

Annexes:

1. Action plan for implementing the Medium Term Microfinance Development Strategy in the Kyrgyz Republic.
2. Analysis of the microfinance sector in Kyrgyzstan.

3. Analysis of legal and regulatory microfinance environment.
4. Meso structure (financial system infrastructure).
5. Overview of technical assistance.